

SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Leno Analyst: LuAnna Hass Bill Number: AB 1690

Related Bills: See Prior Analysis Telephone: 845-7478 Amended Date: July 2, 2003

Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Local General Income Tax/Public Safety Finance Agency

- ☒ DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as amended June 2, 2003.
- ☐ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.
- ☒ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as amended June 2, 2003.
- ☒ FURTHER AMENDMENTS NECESSARY.
- ☐ DEPARTMENT POSITION CHANGED TO _____.
- ☒ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED June 2, 2003, STILL APPLIES.
- ☐ OTHER - See comments below.

SUMMARY

This bill would require the Franchise Tax Board (FTB) to administer and collect a local income tax.

This bill also would add provisions regarding public safety finance agencies and property taxes. These changes do not affect the department and are not discussed in this analysis.

SUMMARY OF AMENDMENTS

The July 2, 2003, amendments resolved the technical concerns and several, but not all, of the implementation concerns discussed in the department's analysis of the bill as amended June 2, 2003. Specifically, these amendments would:

- clarify that FTB would transmit the local income tax within 60 days of the date the personal income tax (PIT) return is processed or FTB collects any unpaid local income tax,
- require FTB to transmit the appropriate penalties and interest attributable to the local income tax to the city or county, or city and county,
- specify that a taxpayer would be considered a resident of a city or county, or city and county, for purposes of a local income tax so long as he or she is a resident of the city or county, or city and county, for at least six months during the taxable year,
- require the city or county to enter into a contractual agreement with FTB to provide for reimbursement of FTB's expenses, instead of FTB being reimbursed through the amounts collected,

Board Position:

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<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Legislative Director

Date

Jana Howard for Brian Putler 07/07/03

- allow FTB to determine an individual's city, county, or city and county of residence in the event the individual fails to include the information on the tax return,
- allow FTB to treat the omission of local income tax as a math error, which would allow FTB to calculate the local income tax, and send a notice of tax due to the taxpayer,
- make technical changes regarding the correct usage of the phrase "income tax," and
- clarify that FTB would be the agency to transmit the local income tax revenues to the cities and counties.

For convenience, the remaining concerns and the fiscal impact are provided below. The remainder of the department's analysis of the bill as amended June 2, 2003, still applies.

POSITION

Pending.

ANALYSIS

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

- This bill would require FTB to estimate, based on historical data, the amount of local general tax to be collected in the first 12 months in which the tax is imposed. Generally, estimating revenue projections is done by a state agency other than FTB, which may have the appropriate information and systems to make such projections. Currently FTB uses zip codes to identify counties for statistical purposes. Zip codes that overlap county boundaries are rare. For purposes of estimating and imposing the city tax in this bill, the use of zip codes would be insufficient because zip codes that overlap jurisdictions are much more common. To appropriately sort tax statistics to incorporated jurisdictions would require complete street address to city cross-reference coding that is not currently in place. The costs described under "Fiscal Impact" below do reflect the cost to create or modify a system to sort tax statistics to the appropriate jurisdictions and estimate the amount of local income tax that could be collected. However, even with a system in place to estimate the local income tax that could be collected, the methodology would be imprecise and could result in substantial errors for specific localities.
- This bill requires FTB to transmit the local income taxes collected within 60 days after collecting the tax. Assuming the taxpayer were to self-assess the local income tax on the PIT return, FTB receives PIT returns and payments daily from January through April 15th or, with an extension, October 15th. In order to ease administration for FTB, the department would likely remit the funds weekly or monthly, which would have a minor impact on current fiscal operations.

FISCAL IMPACT

In order to administer a local income tax program, FTB would incur significant system programming hours. The department would need to create codes and program the systems to identify and calculate the tax for each city, county, and city and county. The calculation of the local income tax would be adjusted in those instances where a mathematical correction is made to a return during processing that would change a taxpayer's PIT liability. The taxpayer would either get a reduced refund or be billed for the additional local income tax. The department also would need to extensively modify the billing system specifically for those taxpayers who do not report or pay the local income tax. All of the information relating to the local income tax would need to be captured and retained in the department's systems. In addition, although a worksheet and instructions would be provided in the PIT booklet, the department anticipates an increase in taxpayer contacts to the department for assistance in calculating the local income tax. Further, there could be an increase in the department's collection activities for those taxpayers who fail or refuse to report or pay a local income tax.

As a result, the department has identified a preliminary implementation cost estimate of \$3.5 - \$3.7 million. Total costs include changes to the tax forms, instructions and booklets, programming, testing, and maintaining departmental systems, processing hours, remittance of the local income tax to the appropriate city, county, or city and county, and the development and negotiation of agreements to ensure taxpayer privacy and non-disclosure of taxpayer information. For purposes of this estimate, the department used the San Diego County population that filed approximately 1.1 million PIT returns. Of the \$3.6 - \$3.8 million estimated above, approximately \$2.4 million is for systems updates and the printing of PIT booklets to include a new worksheet and the various codes. The \$2.4 million cost is not based on the population of a specific city, county, or city and county and would be consistent regardless of the number of cities, counties, or cities and counties that may enact a local income tax. Any cost in excess of the \$2.4 million would be based on the population of a specific city, county, or city and county. Therefore, the department's cost could increase significantly depending on the number and population of cities, counties, or cities and counties that may enact a local income tax.

This bill does not include a provision to cover FTB's start-up costs. To ensure the department has the funding to implement this bill, the department would suggest the author add appropriation language to this bill that would cover the start-up costs of implementation. At a minimum, department staff suggests appropriation language that would provide FTB \$100,000 for the 2003/2004 fiscal year to create or modify a system to estimate the local income tax that could be collected and \$2.3 million for the 2004/2005 fiscal year due to the significant tax forms changes and the programming and testing effort required. The department is currently working on Budget Change Proposals (BCPs) for the 2004/2005 fiscal year and deficiency requests for the 2003/2004 fiscal year. However, absent an appropriation or Department of Finance approval of a BCP for the 2004/2005 fiscal year or a deficiency request for the 2003/2004 fiscal year, the department would be required to redirect staff from other revenue generating activities of the department, such as collections administration or audit, to administer this bill.

ECONOMIC IMPACT

This bill would not impact the state's income tax revenue.

ARGUMENTS/POLICY CONCERNS

This bill would provide inequitable treatment for certain classes of taxpayers. For example, the local income tax under this bill would not be levied against individual taxpayers who do not have a PIT filing requirement or businesses and corporations that reside or do business within the area of the local income tax, even though everyone within the area would realize the benefits of the public safety finance agency.

This bill would authorize the imposition of a local income tax upon the taxable income of any person who is a resident of that locality and the tax may not exceed an amount equal to the net tax multiplied by 8%, 2%, or 10% depending on the taxpayer's locale. For example an individual with taxable income of \$100,000 and one personal exemption would have a PIT net tax of \$7,342. If the taxpayer resided in a city and county that imposed a local general tax of 10%, the local general tax amount would be \$734. However, state tax law allows taxpayers to claim certain tax credits that are used to reduce the taxpayer's tax liability dollar-for-dollar. The taxpayer described above could have credits equaling \$1,000, which would reduce their tax to \$6,342, but their local income tax would still be \$734.

Since this bill does not currently contain a provision to require employers to increase withholding from an employee's (taxpayer's) wages, it is possible that a taxpayer that resides in a city or county that enacts a local income tax would not have sufficient withholding to cover both his or her PIT liability and the local income tax liability for a taxable year. As a result, the taxpayer may be subject to underpayment penalties.

The majority of tax returns are filed on a calendar-year basis. The local income tax would be self-assessed on tax returns filed after the close of that calendar year. For fiscal purposes, ideally, the estimate of local income tax and the collection of the tax would be made for the same taxable year as the tax is assessed on the return. However, the timeliness of the transfer of money to the local jurisdiction may be an issue. Local jurisdictions generally operate on a fiscal year basis. For those returns filed and processed by April 15th the local jurisdiction would likely receive the transfer of tax before the end of one fiscal year. For tax returns filed by the extended due date in October, the local income tax amounts would be transferred to the local jurisdiction in the next fiscal year.

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